



J.D. Agarwal & Aman Agarwal, International Money Laundering in the Banking Sector

International Money Laundering in the Banking Sector

By

Dr. J. D. Agarwal

Professor of Finance,

Founder Chairman, Indian Institute of Finance,

Chief Editor, Finance India

Web: <http://www.iif.edu>; Email: jda@iif.edu

Prof. Aman Agarwal

Professor of Finance &

Officiating Director, Indian Institute of Finance,

Director, IIF Business School (GGS Indraprastha University)

Web: <http://www.iifbs.edu>; Email: aa@iif.edu

Asia Pacific Banking Congress 2004, Century Park Hotel, Manila, Philippines



J.D. Agarwal & Aman Agarwal, International Money Laundering in the Banking Sector



Introduction

- It is estimated that the size of money laundering worldwide through the banking sector, is more than US\$ 500 billion to One trillion annually.
- Money-laundering not only economically destabilizes a country but also exposes it to terrorist attacks, threatening its integrity & sovereignty.
 - Broad international cooperation between law enforcement & regulatory agencies is essential in order to identify the source of illegal proceeds, trace the fund to specific criminal activities & confiscate their financial assets.



Asia Pacific Banking Congress 2004, Century Park Hotel, Manila, Philippines



Introduction

- Money laundering involves bankers, lawyers, car dealers, real estates builders, accountants and also others, who allow their businesses to be used by someone to launder the proceeds of a crime.
- Every country has its criminal underworld. The biggest organizations and the ones that have been active and have long standings can be found in the hubs of capitalism.





J.D. Agarwal & Aman Agarwal, International Money Laundering in the Banking Sector

What is Money Laundering?

- Nefarious activities of the criminals who provide an envelope to “slush funds” in order to exhibit those as genuine money.
- In Black's Law of Lexicon the term laundering is being referred to as investment or other transfer of money flowing from racketeering, drug transactions and other sources (illegal sources) into legitimate channels so that its original source cannot be traced.



Asia Pacific Banking Congress 2004, Century Park Hotel, Manila, Philippines



What is Money Laundering?

- Money laundering generally involves a series of multiple transactions used to disguise the source of financial assets so that these assets may be used without compromising the criminals who are seeking to use the funds
- These transactions fall into three stages
 - Placement
 - Layering
 - Integration





J.D. Agarwal & Aman Agarwal, International Money Laundering in the Banking Sector

Money Laundering: How it is done?

- **Private Bankers as Client Advocates**
 - Private bankers are linchpin of private bank system.
 - They are trained to service their clients, set up accounts and move money around the world using sophisticated financial systems and secrecy tools.
 - Private bankers feel loyalty to their clients leading them to miss or minimize warning signs.
 - Private bankers use their expertise to evade what they may perceive as unnecessary "red tape" hampering the services their clients want, thereby evading controls designed to detect or prevent money laundering.

Asia Pacific Banking Congress 2004, Century Park Hotel, Manila, Philippines



J.D. Agarwal & Aman Agarwal, International Money Laundering in the Banking Sector

Money Laundering: How it is done?

- **Powerful Clients**

- Private bank clients are, by definition, wealthy.
- Many also exert political or economic influence which may make banks anxious to satisfy their requests and reluctant to ask hard questions.
- If a client is a government official with influence over the bank's in country operations, the bank has added reason to avoid offence.
- While private banks routinely claim that their private bankers gain intimate knowledge of their clients, history demonstrate that too often is not true.

Asia Pacific Banking Congress 2004, Century Park Hotel, Manila, Philippines



J.D. Agarwal & Aman Agarwal, International Money Laundering in the Banking Sector

Money Laundering: How it is done?

- **Culture of Secrecy**

- A culture of secrecy pervades the private banking industry. There are layers of secrecy that private banks and clients routinely use to mask accounts and transactions.



- **Secrecy Jurisdictions**

- Private banks also conduct business in secrecy jurisdictions such as Switzerland and Cayman Islands, which impose criminal sanctions on the disclosure of bank information, related to clients.



Asia Pacific Banking Congress 2004, Century Park Hotel, Manila, Philippines



J.D. Agarwal & Aman Agarwal, International Money Laundering in the Banking Sector

Money Laundering: How it is done?

- **Culture of Lax Controls**

- Private bankers are being asked to fill contradictory roles-to develop a personal relationship with a client and increase their deposits with the bank, while also monitoring their accounts for suspicious activity and questioning specific transactions. Human nature makes these contradictory roles difficult to perform.
- Private Banks have dealt with this problem by setting up systems to ensure that private banker activities are reviewed by third parties.

Asia Pacific Banking Congress 2004, Century Park Hotel, Manila, Philippines



J.D. Agarwal & Aman Agarwal, International Money Laundering in the Banking Sector

Money Laundering: How it is done?

- **Cut throat Competition**

- Ongoing competition among private banks for clients, due to profitability of the business.
- The dual pressures of competition and expansion are disincentives for private banks to impose tough anti-money laundering controls that may discourage new business or cause existing clients to move to other institutions.



Asia Pacific Banking Congress 2004, Century Park Hotel, Manila, Philippines



J.D. Agarwal & Aman Agarwal, International Money Laundering in the Banking Sector

Other Factors

- The actual products and services offered by the private bank also create opportunities for money laundering.
 - Multiple Accounts
 - Secrecy Products
 - Movements of Funds
 - Credit
 - Development of Off -Shore Banking



Asia Pacific Banking Congress 2004, Century Park Hotel, Manila, Philippines



J.D. Agarwal & Aman Agarwal, International Money Laundering in the Banking Sector

World's Worst Banking Scandal

- The world's worst banking scandal, of Bank of Credit and Commerce International (BCCI) inflicting huge financial losses on thousands of people worldwide, surfaced in the media in 1991.
- It had heavy ties with the CIA, terrorist organizations, drug traffickers, & other crooked financial transactions shunned by most other banks.
- BCCI started operations in Pakistan in 1972, with much of funding provided by Bank of America & CIA.
- CIA knew about BCCI's activities, & found its mindset to be very manipulating and planned its own operations through BCCI.

Asia Pacific Banking Congress 2004, Century Park Hotel, Manila, Philippines



J.D. Agarwal & Aman Agarwal, International Money Laundering in the Banking Sector

World's Worst Banking Scandal

- CIA Operatives used the bank to launder money from CIA enterprises, including drug trafficking proceeds, & from its various financial activities within the US, to fund unlawful arms shipments, finance terrorist operations, undermine foreign governments & other covert activities.
- Investigating reports showed that :
 - BCCI was able to simultaneously manipulate the spy agencies of numerous countries.
 - BCCI was supplying funds for terrorist Organizations
 - BCCI rigged international commodity markets
 - It was laundering drug money for drug cartels worldwide.



Asia Pacific Banking Congress 2004, Century Park Hotel, Manila, Philippines



J.D. Agarwal & Aman Agarwal, International Money Laundering in the Banking Sector

Frauds from Small Bank Accounts

- The "fraudsters" use fake certificates of deposit drawn on other branches of an international bank, which can range from US\$ 10 million - \$25 million.
- The "fraudsters" also use fund transfers, which involve real dollars, opening up small accounts into which they then pour millions of dollars.
- "Fraudsters" will also use counterfeit letters of agreement, drawn on bank letter heads, seemingly vouching for a client from another branch of that bank, or confirming a deal has been approved etc.



Asia Pacific Banking Congress 2004, Century Park Hotel, Manila, Philippines



J.D. Agarwal & Aman Agarwal, International Money Laundering in the Banking Sector



Frauds from Small Bank Accounts

- The problem which creates a temptation to approve such transactions, is that these banks may be turning away legitimate business. *Thus there is concern that banks operating overseas may be at a competitive disadvantage* because they adhere to standards for “*knowing your customers*” identifying beneficial owners of transactions refusing suspicious or unusual transactions, etc.
- The banks should be advised informally that the answer is not to lower standards in the home country or abroad, but to intensify efforts to ensure that all major financial centers operate within the limits of an international consensus on counter measures.

Asia Pacific Banking Congress 2004, Century Park Hotel, Manila, Philippines



J.D. Agarwal & Aman Agarwal, International Money Laundering in the Banking Sector



What Bankers need to Know: Anti Money Laundering Controls?

- Many important financial centers have now adopted legislation to curb drug related money laundering, and the number of governments which have ratified the 1988 UN Convention continued to increase.
- Banking Industry needs to be one step ahead of money launderers in order to control the menace of money laundering and financial crimes.
- One of the best control techniques for the banks to control money laundering is to know your customer.

Asia Pacific Banking Congress 2004, Century Park Hotel, Manila, Philippines



J.D. Agarwal & Aman Agarwal, International Money Laundering in the Banking Sector



What Bankers need to Know: Anti Money Laundering Controls?

- Eleven world money centre banks agreed in October 2000, to a set of anti-money laundering guidelines - for private banking activities.
- SWIFT, a principal international service for wire transfer message trafficking that can initiate funds transfers by providing services to security bankers and dealers; clearing institutions; and recognized security exchanges
- With organized crime in control of banks & able to launder huge sums of money not only for themselves but also for other criminal organizations.

Asia Pacific Banking Congress 2004, Century Park Hotel, Manila, Philippines



J.D. Agarwal & Aman Agarwal, International Money Laundering in the Banking Sector



What Bankers need to Know: Anti Money Laundering Controls?

- In February 1988, the OECD's Financial Action Task Force- for money laundering in its Annual Report highlighted the problem in Mexico and stated “Corruption remains the chief impediments to Mexican's anti-laundering efforts”
- Under the auspices of UNO, there is an international campaign to crack down on problem of money laundering.
- Now countries have enacted laws to prevent money laundering and allow closer scrutiny of suspect bank accounts of criminals.

Asia Pacific Banking Congress 2004, Century Park Hotel, Manila, Philippines



J.D. Agarwal & Aman Agarwal, International Money Laundering in the Banking Sector



What Bankers need to Know: Anti Money Laundering Controls?

- Government of India has issued anti-money laundering guidelines before introduction of the Prevention of Money Laundering Bill in Parliament.
- Indian Bill embraces money laundering from drug-trafficking, terrorism, profits from prostitution, extortion, smuggled items like gold, diamond etc.
- The Bill in Section 3 deals with this offense and states that whenever a person acquires, owns, possesses or transfers any proceeds of crime or knowingly enters into any transactions or deals or aids the concealment of the “proceeds of crime”.

Asia Pacific Banking Congress 2004, Century Park Hotel, Manila, Philippines



J.D. Agarwal & Aman Agarwal, International Money Laundering in the Banking Sector



What Bankers need to Know: Anti Money Laundering Controls?

- The Bill has the schedule offence which lists 16 sections of Indian Penal Code, 6 Sections of Arms Act, 9 sections of Narcotic Drugs Act and 4 sections of the Prevention of Corruption Act.
- Thus the Bill covers all activities which are capable of producing illegal money.
- The Reserve Bank of India's panel has recommended rules against money laundering.
 - Improving procedures and policies for preparing appropriate (banks) customer profiles & coordination and cooperation with regulatory & other authorities.

Asia Pacific Banking Congress 2004, Century Park Hotel, Manila, Philippines



J.D. Agarwal & Aman Agarwal, International Money Laundering in the Banking Sector



What Bankers need to Know: Anti Money Laundering Controls?

- It also suggested each bank appointed an anti-money laundering compliance officer & create profiles of customers.
- It called for creation of a data bank of suspicious transactions, which could then be circulated to banks to help them detect patterns of suspicious behaviors.
- Infracsoft Technologies has launched a money laundering software in India on the 17th Sept., 2003.
- This is a huge development being India's first globally of adoptable Anti Money Laundering (AML) Software named OMNI Enterprise.

Asia Pacific Banking Congress 2004, Century Park Hotel, Manila, Philippines



J.D. Agarwal & Aman Agarwal, International Money Laundering in the Banking Sector



What Bankers need to Know: Anti Money Laundering Controls?

- US has desired India to play a more aggressive role in its global campaign against terrorism & its financing by joining groups striving to curb money laundering.
- India is yet to join the Paris based Financial Action Task Force consisting of 29 nations which was set up in 1989 to prevent international money laundering.
- Alarmed with reports of money from global terrorist organizations flowing into their account, banks across the globe are implementing special anti-money laundering software to detect unusual flow of money.

Asia Pacific Banking Congress 2004, Century Park Hotel, Manila, Philippines

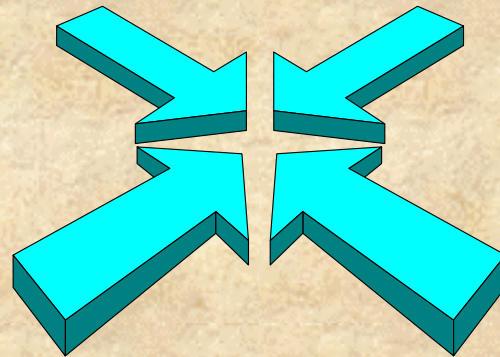


J.D. Agarwal & Aman Agarwal, International Money Laundering in the Banking Sector

Thank you

I must thank the organizers to have given me an opportunity to share my views on the subject.

I must also thank you, ladies and gentlemen, for your kind patience.



Asia Pacific Banking Congress 2004, Century Park Hotel, Manila, Philippines